

Message Text

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USMISSION EC BRUSSELS

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C O N F I D E N T I A L SECTION 01 OF 03 BONN 01314

LIMDIS-GREENBACK

DEPARTMENT PASS TREASURY AND FEDERAL RESERVE

E.O. 11652: GDS

TAGS: EFIN, GW

SUBJECT: VIEWS OF BUNDESBANK VICE PRESIDENT EMMINGER

1. SUMMARY. BUNDESBANK VICE PRESIDENT EMMINGER DURING A CONVERSATION LAST WEEK WITH THE FINANCIAL ATTACHE INDICATED THAT THE BUNDESBANK DOES NOT INTEND TO BUY GOLD, BUT WILL MAKE FURTHER GOLD-SECURED LOANS. EMMINGER FEELS THAT THE GERMAN ECONOMY NOW IS IN A STRONG UPSWING WHICH CALLS FOR A MORE RESTRICTIVE MONETARY POLICY. THE CENTRAL BANK COUNCIL IS SPLIT ON THIS ISSUE, HOWEVER, AND ACTUAL MONETARY POLICY IS LIKELY TO BE NEUTRAL IN THE NEAR TERM. EMMINGER FEELS THAT BASED ON FUNDAMENTAL ECONOMIC FORCES, THE DM PROBABLY SHOULD APPRECIATE BY ABOUT 5 PERCENT DURING 1976, BUT EMPHASIZED THAT THE BUNDESBANK DOES NOT HAVE ANY "TARGETS" OR "TARGET ZONES" FOR THE DM. SOME OF EMMINGER'S REMARKS ARE SENSITIVE. PLEASE PROTECT AND TREAT NOFORN.

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END SUMMARY.

A. GERMAN ECONOMY

2. EMMINGER SAID THAT IN HIS VIEW THE GERMAN ECONOMY IS NOW IN A CLEAR AND STRONG UPSWING. THE MONETARY EXPANSION IS MUCH TOO RAPID AND THE DANGER OF OVER-EXPANSION AND INFLATION FAR OUTWEIGH THOSE OF A "FIZZLING OUT" OF THE RECOVERY. OBJECTIVELY THE BUNDESBANK NOW SHOULD TIGHTEN UP ON MONETARY POLICY. THE PROBLEM IS THAT SUCH A TIGHTENING WOULD FIND ABSOLUTELY NO PUBLIC UNDERSTANDING. PRESIDENT KLASSEN ALSO OPPOSES IT AND FEELS THAT WITH THINGS GOING WELL THE BUNDESBANK SHOULD NOT "ROCK THE BOAT" AND PARTICULARLY NOT ENDANGER THE FINANCING OF PUBLIC DEFICITS BY TIGHTENING MONETARY POLICY NOW. EMMINGER COMMENTED THAT KLASSEN BRUSHES ASIDE MONETARIST ANALYSIS AND INSISTS ON LOOKING AT THINGS "PRAGMATICALLY." WITH THE CENTRAL BANK COUNCIL SPLIT, THE BEST THAT CAN BE HOPED FOR, ACCORDING TO EMMINGER, IS TO STOP ALL FURTHER STEPS TOWARD MONETARY EXPANSION AND LET THE EXPANDING ECONOMY CATCH UP WITH THE MONEY SUPPLY.

3. IN THIS CONNECTION, EMMINGER WAS PARTICULARLY CAUSTIC IN REGARD TO THE ROLE OF THE CDU/CSU OPPOSITION WHICH BY ITS COMMENTS ON THE ECONOMY (DOUBTING THE STRENGTH OF THE RECOVERY) MADE IT THAT MUCH HARDER TO MOBILIZE PUBLIC UNDERSTANDING FOR MORE RESTRICTIVE POLICIES WHILE AT THE SAME TIME BASING ITS WHOLE ELECTION STRATEGY ON A MISTAKEN PROGNOSIS OF THE LIKELY ECONOMIC DEVELOPMENTS BETWEEN NOW AND NEXT FALL.

B. GOLD

4. EMMINGER SAID THAT THE BUNDESBANK HAS NO INTENTION TO BUY GOLD EITHER THROUGH THE BIS OR FROM THE MARKET AND WOULD RECONSIDER THIS DECISION ONLY IF THE GOLD PRICE SHOULD DROP VERY RADICALLY SO AS TO MAKE GOLD A REAL BARGAIN. PRESIDENT KLASSEN HAD JOKINGLY TOLD THE PRESS THAT THE BUNDESBANK MIGHT BUY SOME GOLD IF THE PRICE SHOULD DROP TO \$70 PER OUNCE. WHILE THE

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FIGURE WAS NOT MEANT SERIOUSLY, THIS STATEMENT WAS INTENDED TO DEMONSTRATE THE UNLIKELIHOOD OF ANY BUNDESBANK INTEREST IN BUYING GOLD. EMMINGER THOUGHT THAT WHILE THE GOLD PRICE MIGHT RECOVER AND VARY IN THE \$125 - 145 RANGE, IT WAS HIGHLY UNLIKELY TO GO HIGHER THAN THAT. THE SHOCK OF THE RECENT PRICE DROP HAD DISCREDITED GOLD AS A STORE OF VALUE OR A MEANS OF ASSET DIVERSIFICATION FOR YEARS TO COME.

5. EMMINGER FELT THAT GOLD NOW HAD BEEN EFFECTIVELY
REMOVED FROM THE CENTER OF THE INTERNATIONAL MONETARY
SYSTEM AND WOULD NEVER AGAIN RESUME THAT ROLE. IT
WOULD, HOWEVER, REMAIN PART OF MONETARY RESERVES--TO

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C O N F I D E N T I A L SECTION 02 OF 03 BONN 01314

LIMDIS

BE USED MAINLY AS COLLATERAL FOR LOANS SUCH AS THOSE
THE BUNDESBANK IS CURRENTLY AGAIN IN THE PROCESS OF
ARRANGING.

C. EXCHANGE RATE POLICY

6. EMMINGER SAID THAT HE AND THE BUNDESBANK AGREED
WITH GISCARD'S STATEMENT THAT THE PREVENTION OF
ERRATIC EXCHANGE RATE MOVEMENTS WENT BEYOND THE MERE
PRESERVATION OF ORDERLY MARKET CONDITIONS (WHICH HE
IN TURN DEFINED AS KEEPING DAILY EXCHANGE RATE CHANGES
WITHIN SUCH NARROW LIMITS AS, FOR EXAMPLE, THE ONE
PERCENT PREVIOUSLY AGREED BY THE SNAKE COUNTRIES).
IN HIS VIEW THE PREVENTION OF ERRATIC MOVEMENTS MEANT

THAT IN ADDITION CENTRAL BANKS SHOULD RESIST EXCHANGE RATE MOVEMENTS WHICH WERE CAUSED BY FACTORS OTHER THAN CHANGES IN FUNDAMENTAL ECONOMIC CONDITIONS. THUS, FOR EXAMPLE, HE AGREED WITH GOVERNOR WALLICH THAT IF EXCHANGE RATES RESPONDED TO A CHANGE IN INTEREST RATE DIFFERENTIALS THIS SHOULD BE RESISTED IF THE INCREASED INTEREST RATE DIFFERENTIAL WAS JUST CONFIDENTIAL

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A TEMPORARY ABERRATION AS A CENTRAL BANK TRIED TO GET ITS MONEY SUPPLY UNDER CONTROL. THE EXCHANGE RATE CHANGE, ON THE OTHER HAND, SHOULD NOT BE RESISTED IF THE INCREASED INTEREST RATE DIFFERENTIAL REFLECTED A DECISION BY A CENTRAL BANK TO SPEED UP OR SLOW DOWN THE GROWTH OF THE MONEY SUPPLY OR THE ECONOMY OVER THE MEDIUM TERM.

7. EMMINGER CONTINUED THAT THE BUNDESBANK IN FACT HAD BEEN FOLLOWING THIS POLICY FOR THE LAST YEAR OR SO. IN THIS CONNECTION, HE EMPHASIZED THAT THE BUNDESBANK DID NOT HAVE, AND WOULD NOT HAVE IN THE FUTURE, "TARGET ZONES" FOR THE DM EXCHANGE RATE. SUCH TARGET ZONES COULD NOT BE MAINTAINED AGAINST THE MARKET IN ANY CASE AS THE BUNDESBANK'S MISGUIDED ATTEMPT TO PEG THE LONG-TERM INTEREST RATE LAST SUMMER HAD AGAIN DEMONSTRATED. WHEN HE IN THE PAST HAD SOPKEN OF A "REASONABLE RANGE" FOR THE DM HE HAD ALWAYS TAKEN GREAT CARE TO EMPHASIZE THAT THIS WAS NOT A MEDIUM TERM TARGET, BUT RATHER ONLY A ZONE OF WHAT SEEMED REASONABLE UNDER CURRENT CONDITIONS-- WHICH COULD CHANGE QUICKLY IN THE FUTURE. THE BUNDESBANK TENDED TO INTERVENE SOMEWHAT MORE HEAVILY AS THE BORDERS OF SUCH A "REASONABLE RANGE" WERE APPROACHED, BUT HAD NO INTENTION OF DEFENDING SUCH A RANGE IN A "DO OR DIE" MANNER AGAINST PERSISTENT MARKET PRESSURE. EMMINGER EMPHASIZED THAT HE HAD ORIGINALLY SPOKEN IN TERMS OF SUCH A "REASONABLE RANGE" IN ORDER TO DISTINGUISH IT FROM THE CONCEPT OF A "TARGET ZONE" WHICH HAD ONCE BEEN MISTAKENLY USED IN A PRESS CONFERENCE BY PRESIDENT KLASSEN. (COMMENT: WHILE THE PUBLIC MAY BE CONFUSED BY ATTEMPTING TO DRAW SUCH A DISTINCTION BETWEEN "TARGET ZONES" AND "REASONABLE RANGES", THE GERMAN EXCHANGE MARKET CLEARLY DOES REALIZE THAT THE BUNDESBANK'S "REASONABLE RANGES" ARE MUCH MORE READILY SUBJECT TO CHANGE AND ARE MUCH LESS LIKELY TO BE DEFENDED AGAINST PERSISTENT MARKET PRESSURE. SEE ALSO BONN 826.)

8. WITH THE ABOVE SAID, EMMINGER CONTINUED, THE

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BUNDESBANK IS HAPPY AND CONTENT FOR THE

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C O N F I D E N T I A L SECTION 03 OF 03 BONN 01314

LIMDIS-GREENBACK

TIME BEING WITH THE CURRENT DOLLAR/DM EXCHANGE RATE
OF ABOUT \$1 EQUALS DM 2.59. ON THE BASIS OF
FUNDAMENTAL FACTORS THE BUNDESBANK FEELS THAT THE
DM SHOULD PROBABLY APPRECIATE BY ABOUT 5 PERCENT
DURING 1976 BECAUSE GERMAN UNIT COSTS ARE LIKELY TO
RISE ABOUT THAT MUCH LESS THAN THOSE OF HER TRADING
PARTNERS. BUT, EMMINGER ADDED WRYLY, THINGS NEVER
HAPPEN THAT WAY IN THE ACTUAL MARKET AND 1976 COULD
SEE SOME MAJOR EXCHANGE MARKET STRAINS IF, AS WAS
QUITE POSSIBLE, THE BUNDESBANK WOULD BE FORCED TO
SWITCH TO SEVERE MONETARY RESTRAINT FOR DOMESTIC
REASONS BY NEXT SUMMER OR FALL.

D. INTERNATIONAL MONETARY REFORM

9. EMMINGER (UNLIKE WEBER - SEE BONN 826) WAS GENERALLY PLEASED WITH THE OUTCOME OF THE JAMAICA MEETINGS AND PARTICULARLY FELT THAT LDC ATTEMPTS TO CONVERT THE IMF INTO AN AID AGENCY HAD BEEN SUCCESSFULLY RESISTED BY LIMITING CONCESSIONS AND RESTRICTING THEM TO TEMPORARY RATHER THAN PERMANENT ARRANGEMENTS. HE
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THOUGHT THAT GERMAN PRESS REPORTING OF THE MEETING (SEE BONN 625) HAD GIVEN A VERY DISTORTED PICTURE. UPON RETURNING TO GERMANY HE (AS WELL AS OTHERS) HAD TRIED TO SET THE RECORD STRAIGHT, BUT BY THAT TIME PRESS INTEREST HAD WANED.

10. ONE THING THAT EMMINGER DID FIND WORRISOME, NOT SO MUCH IN REGARD TO THE JAMAICA MEETING AS MORE GENERALLY, WAS THAT WITTEVEEN AND THE WHOLE IMF STAFF "FROM TOP TO BOTTOM" SEEMED TO CONCENTRATE THEIR EFFORTS MORE AND MORE EXCLUSIVELY ON FINDING WAYS OF AIDING LDC'S RATHER THAN THE TRADITIONAL IMF FUNCTIONS.
HILLENBRAND

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